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FILED ELECTRONICALLY

July 15, 2008

Ms. Sandra J. Paske
 Secretary to the Commission
 Public Service Commission of Wisconsin
 Post Office Box 7854
 Madison, WI 53707

**RE: Responses to the Commission's Survey on Innovative
 Utility Ratemaking Approaches that Promote Conservation
 and Efficiency Programs by Removing Disincentives that
 May Exist Under Current Ratemaking Policies.**

Docket 05-UI-114

Dear Ms. Paske:

Northern States Power Company, a Wisconsin corporation (hereafter "NSPW") submits the attached responses to the Public Service Commission of Wisconsin's request for comments, dated June 3, 2008, regarding innovative utility ratemaking approaches that promote conservation and efficiency programs by removing disincentives that may exist under current ratemaking policies.

If you have questions regarding this filing please contact me at (715) 838-4012 or via e-mail at karl.j.hoesly@xcelenergy.com.

Sincerely,

/s/

Karl J. Hoesly
 Manager, Regulatory Affairs

cc:	Donald F. Reck	Xcel Energy
	Deb Sundin	Xcel Energy
	Suzanne Galster Doyle	Xcel Energy
	Amy A. Leberkowski	Xcel Energy
	Donald R. Dahl	Xcel Energy
	Jean A. Derfus	Xcel Energy

Attachment

**OFFICIAL FILING BEFORE THE
PUBLIC SERVICE COMMISSION OF WISCONSIN**

Responses to the Commission's Survey on Innovative
Utility Ratemaking Approaches that Promote Conservation
and Efficiency Programs by Removing Disincentives that
May Exist Under Current Ratemaking Policies.

Docket 05-UI-114

**NORTHERN STATES POWER COMPANY'S, A WISCONSIN CORPORATION,
COMMENTS ON A PSCW REQUEST FOR COMMENTS DATED JUNE 3, 2008**

- 1. Do the current rate structures of the electric and gas utilities in Wisconsin contain a net lost revenue and profit effect that is significant enough to discourage these utilities from developing and spending additional money on energy efficiency programs?**

Response: The current rate structure uses escrow accounting for conservation expenditures coupled with biennial rate cases. Energy efficiency efforts reduce sales between rate cases causing a decrease in the contributions to fixed margins that would have been collected through these lost sales. Given Wisconsin has biennial rate cases these losses are contained and therefore the current structure does not provide a significant disincentive to the current level of energy efficiency efforts. However, the current rate structure depends on energy sales for recovery of both fixed and variable costs, therefore increases in the amount of energy efficiency do have an effect on sales and lost margin recovery. This may discourage utilities from spending additional money on energy efficiency programs.

- 2. (Question for utilities) Is your utility likely to propose energy efficiency spending above current levels if any disincentive to do so is removed?**

Response: Removing any disincentive that results from energy efficiency is not the only factor that needs to be considered in determining whether NSPW would propose increased energy efficiency spending. In addition, NSPW would need to review and agree that the costs, benefits, and amount of increased energy efficiency savings of additional programs are needed in addition to the already available energy efficiency programs.

- 3. If disincentives are removed and the utility elects to spend higher than current amounts on energy efficiency is it best for (a.) the utility to develop and implement the programs; (b.) should that be done by Focus on Energy; (c.) should it be done through a combination of the utility and Focus on Energy; or (d) should it be done by some other entity?**

Response: Both models have had success and there is probably not an easy answer on how the State should proceed if the decision is to considerably expand the amount of energy

efficiency that is achieved by these programs. Issues that should be considered when making this decision include:

- Is the Focus on Energy business model successful in obtaining cost-effective achievements across all customer sectors and serving all customers across the state of Wisconsin?
- Can the Focus on Energy business model be successfully expanded to meet additional goals or are there areas of strengths and weaknesses that should be assessed?
- Is the State still interested in having consistent programs across the state or would they allow for differences between programs delivered by utilities?
- If a combination of programs are provided by utilities and Focus on Energy, how do we design this system to eliminate duplication of services or market confusion?

Xcel Energy has been comfortable with the Public Benefits model in Wisconsin but if this is the model chosen to deliver expanded energy efficiency programs we would like to be assured that we would continue to receive timely cost recovery, and the lost margin issue be reviewed within the current rate structure.

4. Do utilities currently have the resources to develop and implement additional energy efficiency programs?

Response: Xcel Energy provides energy efficiency programs in Minnesota, Colorado, New Mexico, North Dakota and Texas; as a result we have a knowledgeable central staff on developing and marketing energy efficiency programs. However, this staff would require expansion if we agreed to expand our efforts into Wisconsin. As a result of the transition to Focus on Energy, we have downsized or eliminated local Wisconsin support for these efforts. This local support especially in the customer interface and sales areas would need to be redeveloped and trained.

5. Should a decoupling mechanism consider only the effects of additional energy efficiency spending or should it also include the effects of other factors such as the economy and weather on actual vs. forecasted sales? If yes, please explain why?

Response: No, it would not be necessary to limit a decoupling mechanism to the effects of additional energy efficiency. There is a range of options for decoupling mechanisms, ranging from a narrow to broad focus. For example, if a mechanism were narrowly focused on energy efficiency it may eliminate the perceived disincentive for a utility to advocate additional energy efficiency, but it may be difficult to measure. While a more broad approach to a decoupling mechanism may be easier to measure and track, it may be controversial on its own merit.

6. If you answered yes to Question #5, should it be necessary for a utility to propose additional energy efficiency spending before it could seek recovery of any lost revenues due to other factors?

Response: NA – see question 5.

- 7. If a decoupling mechanism considers only the effects of additional energy efficiency spending, but due to weather, economic, or other factors the overall sales are equal to or greater than forecast, or if due to other factors the utility is either earning its authorized ROE or is within some range of its authorized return, should it still recover lost revenues?**

Response: Yes. A mechanism narrowly focused on energy efficiency such as the mechanism described above should not consider factors other than energy efficiency. The purpose of such a mechanism is to isolate only the effects of energy efficiency on sales. It is not appropriate to consider the effect of other factors such as weather, economics, or other factors.

Also as stated in the response to Question 14, NSPW does not believe a formulaic approach to decoupling is retroactive rate making. However, coupling a formulaic approach with an after-the-fact ROE test could, arguably, be considered retroactive ratemaking.

- 8. Please provide what you believe to be the key components of a decoupling mechanism.**

Response: As mentioned earlier, there is a range of decoupling options available. However, the most easily administered is the mechanism with a relatively simple calculation, easily understood by both the customers and the Commission.

- 9. Please provide examples of ratemaking mechanisms other than decoupling that could incent utilities to pursue additional energy efficiency spending at a reasonable cost to ratepayers.**

Response: There are three areas we believe need to be addressed when utilities are requested to transition from a supply side model to a model that includes significant energy efficiency goals: 1) cost recovery, 2) lost margin recovery and 3) earnings incentive mechanism. Decoupling is designed to make a utility neutral to lost margins. There are ways to design a mechanism to provide recovery of lost margins directly without going to a decoupling mechanism. These types of mechanisms were in existence in the 1990's. With some changes they can be re-designed to meet today's needs. Another option that can be looked at is a mechanism that provides a performance incentive.

These other incentives are normally based on a utility's performance in reaching certain savings goals. These mechanisms often include incentives based on sharing or retaining of some percentage of the net economic benefits of the programs, incentives based on a percentage of additional spending, incentives that provide an increased rate of return on the investments in energy efficiency such as a returns equal to the return on supply-side investments.

The downside to these mechanisms is that they don't always provide enough value to the utility to recover all of their lost margins and if the utility does not meet the goals that lead to an incentive payout, the lost margins generated by the lower achievement are not recovered.

A straight fixed variable rate design, or moving from volumetric towards fixed charges for distribution service, would help to remove the disincentive for a utility to promote energy

efficiency. It would also eliminate the rate discrimination against customers living in older homes as well as help to mitigate the price volatility in winter heating months. Allowing a utility to deduct the forecasted energy efficiency savings from their test year sales would also help to remove the disincentive for a utility to promote energy efficiency

10. Should all customer classes be included in any mechanism that is implemented to encourage utilities to promote additional energy efficiency spending? Why or why not?

Response: If a decoupling mechanism is narrowly focused on just energy efficiency then all classes could be included. However, larger customers have more incentive to pursue energy efficiency.

In a broader focused mechanism, including factors such as weather and decreasing use per customer, NSPW would recommend limiting the mechanism to residential and small commercial customer classes. The larger classes may have usage changes that are not associated with weather or energy efficiency but may be due to shutting down a machine, closing a section of the plant, adding a machine, etc.

11. If your answer to Question #10 is no, should additional energy efficiency programs only be designed to benefit only participating customer classes? Why or why not?

Response: Not necessarily. Each energy efficiency program should be evaluated on its own merit. A promising program should not be abandoned because of perceived disincentives.

12. Do you foresee controversy in determining the amount of reduced kWh sales caused by additional energy efficiency spending and the dollar margin on the reduced sales used to determine the under recovered amount to be included in rates? Why or why not?

Response: Yes. Determination of reduced therms or kWh sales due to energy efficiency could be a calculation that may become a contested issue in a rate case proceeding.

13. Considering the lag time between the design and implementation of energy efficiency programs and that utilities file regularly for rate reviews, would the following alternative to decoupling be useful in removing disincentives to utilities promoting these programs? From programs that a utility is proposing prior to a rate case filing an estimate of reduced sales would be made and the test year sales forecast would be reduced accordingly. For programs developed and implemented during the utility's biennial period, a decoupling mechanism could be used to adjust for the impact of these programs until the next rate period (it would be likely that the lag time in implementing programs would make revenue adjustments relatively small).

Response: This method could be useful in removing disincentive to utilities promoting energy efficiency. On its face it appears to insulate the utility from reduced kwh/therm sales due to energy efficiency programs. It would be important with a mechanism such as this to

isolate the energy efficiency impact and not include the differences in sales verses forecast attributed to other causes.

14. Is revenue decoupling illegal retroactive ratemaking? Why or why not?

Response: Whether revenue decoupling constitutes retroactive ratemaking will depend entirely on the decoupling method ultimately adopted by the Commission. As a result the Commission should carefully consider the retroactive ratemaking issue as it deliberates the question of which decoupling mechanism to adopt. One possible approach, which will avoid retroactive ratemaking issues, is the use of a formulaic methodology. If decoupling adjustments were made prospectively through a mathematical formula adopted in a final rate order retroactivity would not be an issue. Such a methodology would be similar to the purchased gas adjustment that gas utilities have used for decades.

Also as stated in the response to Question 7, NSPW does not believe a formulaic approach to decoupling is retroactive rate making. However, coupling a formulaic approach with an after-the-fact ROE test could, arguably, be considered retroactive ratemaking.

15. Are you aware of mechanisms other states use to incent additional energy efficiency on behalf of their utilities that you believe would be successful in Wisconsin? If so, please identify those states.

Response: There are many states that use other mechanisms, such as listed in response to #9, to incent additional energy efficiency. A report from ACEEE entitled, “*Aligning Utility Interests with Energy Efficiency Objectives: A Review of Recent Efforts at Decoupling and Performance Initiatives Report*”, lists many of those states and their incentive mechanisms. In addition, since this report was published in 2006, there are even more states that have enacted laws with performance incentive mechanisms or are allowing for such mechanisms to be designed and implemented in upcoming rulemakings or DSM dockets. Three such states in which Xcel Energy operates are Texas, Colorado, and New Mexico.

Link to the above referenced report:

<http://www.aceee.org/store/proddetail.cfm?CFID=16081&CFTOKEN=77510431&ItemID=421&CategoryID=7>

16. Does a decoupling mechanism represent a reduction in risk to the utility? If so, should that be reflected in the authorized return on equity?

Response: A narrow decoupling mechanism restricted to energy efficiency would have an insignificant effect on risk. A broader decoupling mechanism may provide protection against a decline in sales, but it also eliminates any upside from greater than expected sales. It would be hard to convince investors that it makes sense to accept a lower ROE, when they are giving up the potential upside. Further, since Wisconsin has a requirement to file a rate case every other year and uses a forward test year, the impact of any decoupling may not be that significant on the revenue stream. It is imperative that a utility must maintain favorable credit rating in order to attract capital and efficiently participate in capital markets.

17. What process should the Commission use to establish the parameters of ratemaking approaches that promote energy efficiency; i.e., should the Commission approve utility-specific plans or establish guidelines for implementation in rate cases?

Response: While some specific guidelines, designed in a cooperative technical conference might be useful, the ultimate decision on whether specific action like a decoupling mechanism should be left to general rate cases.

18. Are there important differences between gas and electric utilities to be considered when designing an incentive mechanism?

Response: Yes, depending on the mechanism adopted, there may be significant differences between gas and electric utilities. The primary difference is driven by the impact weather has on natural gas sales compared to electric sales, as well as the demand destruction the natural gas utilities are experiencing.